

GENERAL AGREEMENT ON TARIFFS AND TRADE

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REPORT OF THE COMMITTEE ON BALANCE-OF-PAYMENTS RESTRICTIONS
ON THE CONSULTATION UNDER ARTICLE XVIII:12(b) WITH

P A K I S T A N

1. In accordance with its terms of reference, the Committee conducted the consultation with Pakistan under Article XVIII:12(b). The Committee had before it: (a) a basic document (MGT(60)74), including, as an annex, the Pakistan Government Gazette of 24 June 1960 setting out the licensing schedule for the second half of 1960; (b) a General Statement by the Government of Pakistan on the Policy regarding the use of import restrictions for balance-of-payments reasons (MGT(60)72); and (c) documents provided by the International Monetary Fund, as mentioned in paragraph 2 below. In conducting the consultation, the Committee followed the "Plan" recommended by the CONTRACTING PARTIES. The consultation was completed on 28 October 1960. The present report summarizes the main points covered in the discussion.

Consultation with the International Monetary Fund

2. Pursuant to the provisions of Article XV of the General Agreement, the CONTRACTING PARTIES had invited the International Monetary Fund to consult with them in connexion with this consultation with Pakistan. In accordance with the agreed procedure, the representative of the Fund was invited to make a statement supplementing the Fund's documentation concerning the position of Pakistan. The statement made was as follows:

"The International Monetary Fund has transmitted to the CONTRACTING PARTIES the Executive Board decision relating to the last consultation with Pakistan under Article XIV of the Fund Agreement¹ and the background material prepared in connection with that consultation. The Fund has also provided a supplementary paper, dated September 21, 1960, to supply background information on recent developments.

"With respect to Part I of the Plan for Consultations, relating to balance of payments position and prospects, and with respect to Part III, relating to system and methods of the restrictions, since the conclusion of the last consultation under Article XIV of the Fund Agreement on November 4, 1959, Pakistan has made progress in reducing restrictions. The Fund will shortly consult with Pakistan, and expects to transmit to the CONTRACTING PARTIES the Executive Board decision relating to that consultation when it becomes available.

¹See Annex II

"With respect to Part II of the Plan for Consultations, relating to alternative measures to restore equilibrium, pending the conclusion of its next consultation with Pakistan, the Fund has no comments on alternative measures."

Opening Statement by the Representative of Pakistan

3. The following is a brief resumé of the opening statement made by the representative of Pakistan, the complete text of which is attached as Annex I to this report. The economic situation in Pakistan had shown important gains in certain sectors in 1959/60. Agricultural production had increased. Industrial production had risen more rapidly than in the previous year, and this rise had permitted larger exports of manufactured goods, contributing quite significantly to the rise in foreign exchange receipts. The current account surplus increased from Rs.13.6 million in 1958/59 to Rs.127 million in 1959/60. The gold, dollar and sterling reserves had risen by Rs.126 million to Rs.1170 million, notwithstanding some liberalization of imports. The year also witnessed a significant advance towards the freeing of the economy from price and distribution controls. On the other hand, money supply had increased substantially, leading to a significant rise in prices and the cost of living. The rise in money supply had occurred notwithstanding the absence of deficit spending by the Government which had this year avoided borrowing from the State Bank, and had been occasioned largely by the monetization of the balance-of-payments surplus. A rise in bank credit to the private sector was mainly associated with higher levels of imports. The rise in prices reflected a shortage of supplies in relation to effective demand.

4. Even in sectors of the economy showing improvement, there were certain underlying trends which suggested that complacency was unwarranted. The increase in food production was the result mainly of favourable weather conditions and crop substitution. Earnings from the basic exports of Pakistan, jute and cotton, actually declined by Rs.80 million in 1959/60, and the improvement in exports of manufactured goods had been mainly due to the Export Bonus Scheme which could at best be considered a temporary expedient. Furthermore, the improvement in the balance of payments in 1959/60 as a whole concealed a significant reversal of the favourable trend in the second quarter of 1960.

5. The representative of Pakistan stated that his Government considered it to be of vital importance to concentrate on objectives which would bring about lasting improvements in the economy and in the balance of payments through consistent and integrated economic policies, and described in detail the principal factors and considerations relevant to these long-term objectives.

Balance-of-Payments Position and Prospects

6. Members of the Committee thanked the representative of Pakistan for his comprehensive and informative statement. They noted with satisfaction the improvement in the economy of the country resulting in a more favourable balance-of-payments position. They welcomed the import liberalization measures and the non-discriminatory policy followed in the application of remaining restrictions. They welcomed the courageous readiness which the Government of Pakistan had shown to deal with the balance of payments disequilibrium by taking suitable internal economic measures, and noted the fundamental policy of increasing production and the long-term measures of economic development.

7. Some members of the Committee referred to the statement of the Pakistan representative that there had been a reversal in the favourable trend in the balance of payments in the second quarter of 1960, and enquired as to any forecast the Government might have made regarding future prospects. In reply to this and other questions the representative of Pakistan advised the Committee that such forecasts were very difficult for a country like Pakistan whose economy was directly affected by fluctuations in prices of primary products on world markets and on the vagaries of nature. The fall in the prices of Pakistan's exports was not compensated by any commensurate fall in import prices. The set-back in the second quarter of 1960 was, however, partly attributable to seasonal factors. The general feeling of his Government was one of cautious optimism; the situation would become clearer at the end of the first quarter of 1961, at the end of the next jute and cotton season. If foreign exchange receipts remained stable and the reserves further increased in the first half of 1961 it would not be unlikely that his Government would consider undertaking a further liberalization since it was the declared policy of his Government to proceed with liberalization as quickly as possible, but he was not in a position to make any definite statements in this regard at the present time. Referring to the General Statement by the Government of Pakistan which attributed part of the decline in reserves in the second quarter of 1960 to a gold payment to the I.F. in connexion with the increase in Pakistan's Fund quota, a member of the Committee pointed out that Pakistan had drawn an equivalent amount from the Fund during the third quarter of 1960 so that for the year as a whole the Fund transactions would have no effect on the level of gross reserves.

8. A member referred to the recent sharp rise in the price of jute. Asked to comment on this development, the representative of Pakistan explained that it was the policy of his Government to maintain an adequate supply of raw jute for both domestic and foreign consumption at a price level which would at the same time encourage producers and sustain demand. He mentioned that the previous practice of fixing the amount of acreage under jute cultivation had been discontinued in January 1960. With respect to cotton, the policy was to keep prices at a level which would encourage the production of yarn and cloth. It was planned to increase cotton production by improving the yield per acre which at present was one of the lowest in the world. The prospects for cotton seemed to be favourable for the 1960 season.

Alternative measures to restore equilibrium

9. A member of the Committee noted from the opening statement of the Pakistan delegation that, despite the avoidance of government borrowing from the State Bank, a sharp increase in the money supply had occurred due in part to an increase in bank credit to the private sector. He noted that in order to reduce inflationary pressure a tight monetary policy had been encouraged by raising the Bank Rate from 3 to 4 per cent in the middle of January 1959, and that this had been followed by certain selective credit control measures in March 1960 with a view to checking extensive credit expansion in certain sectors. He asked for details of these selective control measures and their results. The representative of Pakistan replied that, as a disinflationary measure and with a view to checking the hoarding of imported goods and directing credit to more essential purposes, credit restrictions had been imposed on bank advances. Banks were required to limit the granting of advances for unsecured advances for imports of manufactured goods (except industrial machinery, iron and steel) and cotton yarn (except for export) to 60 per cent of the value of such goods, and advances secured by guarantee to a maximum of Rs.50,000.

10. A member suggested that in the face of the inflationary pressures which had been reflected in high demand and shortages, it might be helpful if imports of consumer goods were further liberalized. The representative of Pakistan noted with interest this suggestion and informed the Committee that Rs.50 million were released in the January/June 1960 shipping period especially for consumer goods items with the result that prices fell all round and that this policy was followed during the current July/December shipping period when twenty-eight items were placed on automatic licensing, most of which either pertained to finished consumer goods or were raw materials for the local manufacture of consumer goods. Another member of the Committee noted that while liberalization of imports should in general be welcome, in the present case the conservation of monetary reserves might well limit freedom of further action. He suggested that monetary measures might be a more direct method of dealing with the present difficulties of Pakistan which appeared to have some direct connexion with the rate of expansion of money supply.

11. Members of the Committee expressed interest in the progress made by Pakistan under its two Five-Year Development Programmes, and asked what effects they might have had on exports. The representative of Pakistan advised the Committee that the primary aim of the new Five-Year Plan was the attainment of self-sufficiency in certain essential products. The plan envisaged a total expenditure of Rs.19,000 million. Some of the principal goals were to increase national income, to increase the production of food grains so as to attain self-sufficiency in these products by the end of the period, to increase industrial production of both small and large-scale industries and to accelerate the economic development of the less-developed areas of the country. While the statistics available thus far might reflect insufficient progress in some sectors, there had been substantial progress in others.

The experience obtained in executing the Plan would contribute to future progress in economic development. While the main target of the Plan was to achieve self-sufficiency in food production it was also the intention of the Government to promote, in so far as possible, the expansion of exports.

12. One member of the Committee asked to what extent the Government felt that the growing dependence on foreign aid referred to in the General Statement by the Pakistan Government gave rise to an element of uncertainty. The representative of Pakistan replied that in most cases foreign aid appropriations were made on an annual basis while the commitments relating to the programme of economic development had to be planned over longer periods of time, but this was no longer a very serious problem in the light of the experience gained in planning. He stated that dependence on foreign aid and grants would continue to be a major source of development financing and that the level of aid would be the principal factor in deciding the size of future development programmes.

System and methods of restriction

13. Members of the Committee welcomed the import liberalization measures initiated on 1 July 1960. A member of the Committee expressed concern at the fact that under the present procedures the base period chosen for allocating licences was the year 1952, at which time his country had not entered the Pakistan market for such goods as machinery. Considering the abnormal circumstances of the early post-war years, he suggested that a later period should perhaps be chosen for the purpose of issuing licences in future. Furthermore, the Registration (Importers and Exporters) Order of 1952 provided that all importers and exporters must register themselves with the Chief Controller of Imports and Exports before they were permitted to engage in trade. He pointed out that this practice constituted a certain limitation on imports from countries which had not established extensive trade channels in Pakistan. The representative of Pakistan informed the Committee that the base period of 1950/52 was used only to determine the entitlement of the prospective importer. It was not possible to choose any later period as the O.G.L. was cancelled in 1952 and imports were restricted. The restriction of the entitlement to the performance of the importer during the O.G.L. period, which was used as a unit for licensing, did not preclude the importer from going to sources for supplies which were not open to him during the base period. Many countries that were not suppliers of goods to Pakistan in 1952 were now selling in the Pakistan market as a result of their salesmanship and quality-cum-price of their products. Similarly the Registration (Importers and Exporters) Order 1952 did not place any restrictions on the sources of supply or the countries from which the importer should obtain supplies. However, as the balance-of-payments position was improving new importers were being admitted, and in the Import Policy announced on 24 June 1960 new importers were being established in eighteen items, mostly of daily consumer and industrial use, e.g. books, X-ray films, dyes, chemicals, etc. All contracting parties did have the chance of introducing their products through this fresh medium.

14. The same member of the Committee noted that under the scheme for "new-comers" only persons or firms fulfilling prescribed conditions might apply for licences to import specified items and that this prevented other than established importers from participating in the trade. He asked if it was intended to expand the scope of imports permitted under this scheme. The representative of Pakistan explained that the purpose of this scheme was to enable those in the less-developed areas of the country who were not at present established importers to participate in the import trade. He explained that applications were considered individually on their merits and those in the trade were admitted for direct imports as well.

15. Several members of the Committee expressed interest in the operation of the Export Bonus Scheme which appeared to have provided the largest contribution to the rise in foreign exchange receipts in 1959/60 by encouraging the export of manufactured goods. One member of the Committee noted that the Official Gazette of Pakistan, circulated to the Committee, published lists of goods that could be imported under the regular licensing schedule and wished to know to

what extent these lists corresponded to the 227 items which could be imported with exchange retained under the Export Bonus Scheme. The representative of Pakistan explained that there was a certain amount of over-lapping between the lists under reference.

16. In reply to other questions, the representative of Pakistan stated that this scheme was considered to be only a temporary expedient and that the Government was aware of its inherent deficiencies. The experience gained in relation to cotton yarn, which had been placed under the scheme last year, might be noted. When exports of cotton yarn began to increase the home market experienced shortages, consequently action had to be taken to halve the original bonus entitlement and at the same time to control and reduce the domestic prices of both yarn and finished products. This experience had shown that the new measure, by strengthening the export incentive and thereby rendering the internal market less attractive could present its own problems. In this case it had ultimately been necessary to request individual textile mills to supply a prescribed quantity of yarn to the domestic consumer. Similar developments had been experienced with respect to exports of tea.

17. A member of the Committee noted that exporters of the goods covered by the Export Bonus Scheme were given bonus vouchers for different percentages of the f.o.b. value earned which entitled them to import certain specified goods, including industrial raw materials. The documents before the Committee seemed to indicate that the exporters receiving the vouchers were entitled to sell them to importers. The member asked for confirmation of this information and asked how the prices for them were established. The representative of Pakistan affirmed that the vouchers could be transferred and the holder could charge any consideration for this transfer. The price of the voucher therefore varied from time to time depending upon their availability and the shortage and essentiality of the goods which could be imported against them. No control was exercised by Government on these transactions. Another member of the Committee called attention to the dangers inherent in such a system, especially where it was retained over a long period of time. He understood that in August 1959 the premium for these vouchers stood at about 160 per cent but that this rate might fluctuate between 130 and 200 per cent. He asked for details regarding the present rate of the premium. The representative of Pakistan informed the Committee that the premium since the announcement of the current liberal import policy had ranged between 120 to 150 per cent. He added that there had been instances in which complaints were raised against importers who were charging inordinately high prices for products imported under the scheme on the pretext of additional cost involved in the purchase of the entitlement vouchers, and that his Government had taken steps to remedy this situation. Items of daily use or of necessity had been put on automatic licensing so that there would be no occasion for their importation under bonus vouchers. Furthermore, some other items had been removed from the bonus list and adequate imports were being allowed through normal import licenses.

18. A member of the Committee expressed concern over the fact that Pakistan maintained barter arrangements and several bilateral trade agreements. The representative of Pakistan noted in this connexion that although there could be no doubt about the desirability of conducting trade and payments on a

multilateral basis, Pakistan was faced with special difficulties as a result of its reliance on a few export commodities. Members of the Committee commented that, although it was understandable that Pakistan in its present balance-of-payments position should try to avail itself of all possible trading opportunities, the reliance on bilateral agreements, especially those involving single country licensing or barter arrangements, had inherent serious disadvantages. Imports from bilateral sources could be substantially more costly in terms of foreign exchange than similar imports from other countries. The representative of Pakistan said that trade agreements not involving bilateral quotas were in force with a number of countries. He added that where barter arrangements had been entered into a certain degree of discrimination was unavoidable but the relative volume of imports was negligible. A member of the Committee called attention to a statement made by the Pakistan Minister of Finance in January 1960 to the effect that it was the intention of the Government to conclude specific arrangements with individual countries in order to sell cotton, jute, tea and certain other commodities. Requested to comment on this statement, the representative of Pakistan said that in his country all trade was conducted on commercial terms as all importers were free to decide from which source they would import, and that this freedom was not impeded by bilateral agreements except in one isolated case. Probably less than 2 per cent of Pakistan's total trade was conducted under single country licences. In most of these cases, the agreement was general in nature, providing for no quotas, but merely indicative commodity lists. Only in the case of the agreement with Japan was there a commitment to use single country licences; the agreement provided that Japan would permit Pakistan raw cotton to be imported on equal terms within the sterling quota for cotton, and that Pakistan would issue single country licences in favour of specified Japanese exports if Japanese imports of Pakistan raw cotton reached an agreed quantity.

19. A member of the Committee considered that the inclusion of lists of goods with quantities shown, whether these be referred to as "targets" or "estimates" of trade, inevitably had a diversionary effect on trade. These "targets" or "estimates" could not fail to affect administrative decisions relating to the issue of licences or the allocation of quotas to importers. In this connexion the representative of Pakistan pointed out that in no agreement except that with Japan was there any commitment regarding targets or estimates of trade. All import licences issued in Pakistan, regardless of what general trade agreements were in force, were valid for imports from all countries; hence he did not feel that there could be any likelihood of indirect discrimination arising. The representative of Pakistan stated that his Government was fully aware of the desirability of conducting trade and payments on a multilateral basis. He assured the Committee that although his Government was constantly striving to reduce reliance on bilateralism, in the interim it was necessary to maintain certain arrangements in order to diversify or establish export markets.

20. A member of the Committee pointed out that although the amount of commodities entering Pakistan under barter arrangements was small, the few commodities involved could conceivably be of importance in the overall trade pattern of certain exporting countries. He suggested that where such arrangements existed consideration should be given to licensing similar items fairly freely from all sources in order that exporters in other countries might be provided with an opportunity to compete in the market. The representative of Pakistan assured the Committee that this point was kept constantly under review by his Government and that it would continue to be taken into account.

He explained that barter arrangements were usually made to meet an urgent necessity during a season to dispose of certain primary products which would otherwise not be sold. A member of the Committee welcomed this encouraging clarification of Pakistan's purpose in the use of barter trade, and expressed the hope that this would continue to be the policy followed by the Government of Pakistan.

21. A member of the Committee observed that 20 to 30 per cent of Pakistan's total trade was under State trading. He asked if all countries had an equal opportunity to participate in providing imports under State-trading operations. The representative of Pakistan replied in the affirmative; State trading was conducted purely on the basis of commercial considerations, in accordance with Article XVII.

22. A member asked whether Pakistan maintained a prohibited list. The Pakistan representative stated that there was no prohibited list but that since under the Import Control Act no goods could be imported on a commercial basis without an import permit or licence, all items that were excluded from the importable list announced with the import policy became automatically prohibited. Some of these items, however, were permitted to be imported under bonus vouchers (such as liquid gold, long-playing records, toilet articles and perfumery concentrates). A member of the Committee asked if Pakistan could permit token imports by establishing small quotas for these goods so that they would be permitted to enter Pakistan in minimum commercial quantities. The representative of Pakistan replied that the Export Bonus Scheme was intended to permit such imports and that if demand justified the imports could be made in any quantity under this arrangement.

Effects of the restrictions

23. Members of the Committee observed that the system of restrictions used by Pakistan might have an undesirable effect on the country's economic development in the long run because of the diversion of factors of production to less economic uses, consequently impeding Pakistan's ability to compete in export markets. They drew attention to the 1959 IMF decision which, among other things, urged the Government of Pakistan to consider policies which would reduce reliance on restrictions. The representative of Pakistan explained that his Government was aware of the possible adverse effects on economic development and efficiency of the continued use of restrictions over a long period. The restrictions were, however, indispensable at present in view of the need to protect the balance of payments. While the development programme envisaged self sufficiency in certain sectors his Government fully recognized the benefits to be derived from competition, and would constantly endeavour to minimize the incidental protective effects of the restrictions.

General

24. Members of the Committee thanked the representative of Pakistan for the information supplied to the Committee and the answers given to the various questions. The Committee congratulated the Government of Pakistan on the

improvement in the economic situation in Pakistan and welcomed the internal monetary and fiscal measures taken with a view to restoring equilibrium. The Committee welcomed the recent liberalization in import restrictions, and expressed the hope that further improvement in Pakistan's balance-of-payments position would enable continuing progress in this regard. They further expressed the hope that Pakistan would reduce reliance on bilateral agreements, especially those involving single country licensing.

25. The representative of Pakistan stated that he had taken note of the views expressed and suggestions made by members of the Committee and assured the Committee that these would be conveyed to his Government which would undoubtedly give the careful and sympathetic consideration.

ANNEX I

Opening Statement by the Representative of Pakistan

My Government has always found it most interesting, for our sake as well as in wider interests, to participate in exercises such as these. I was myself a member of this Committee two years ago, and the reason why we have not sought representation on it over the last two years is certainly not any lack of interest or any idea that we cannot learn by listening to such debate but rather to the fact that we simply have not the manpower to spare. This Committee has had a very full experience of the problems confronting the less-developed countries, and such shortage of manpower, to which I have referred, is only one symptom of what it means to be, in the language which we use here, a less-developed country. The other symptoms have no doubt become or will become apparent in these consultations. I have been impressed by the spirit of reality, coupled with that of sympathy and of understanding with which this Committee has approached its task in the past, and I will do my best in return to afford frank and full answers to all questions that will be put to me.

I am instructed by my Government to thank the IMF and the secretariat for the fairly comprehensive documentation which is before us all. I will endeavour to relate something of the latest position in my country, trying not to repeat what is written in the documentation already studied by the Committee.

My information is as late as September 1960. Our findings last month were that the economic picture over twelve months has shown important gains in certain sectors. Agricultural production has shown a rise, which was very welcome. The output of rice was at its highest since 1947. Wheat production increased for a second year in succession. The output of coarse grains was also higher in the general sense. Among non-food crops, production of cotton rose by nearly 6 per cent. Industrial production rose more rapidly than last year. A higher industrial production made possible larger exports of manufactured goods, and this in turn contributed quite significantly to the rise in foreign exchange receipt. The current accounts surplus in the balance of payments increased from Rs.1.36 crores (1 crore is equal to ten million) in 1958-59 to Rs.12.72 crores in 1959-60. The gold, dollar and sterling reserves rose by Rs.12.65 crores to Rs.116.96 crores. The increase in reserves took place notwithstanding a certain degree of liberalization in imports on private account. The twelve months also witnessed a significant advance towards the freeing of the economy from price and distribution controls. Wheat rationing was abolished throughout West Pakistan and all restrictions on the movement and distribution of wheat, except in a border belt, were removed. In East Pakistan, statutory rationing was abolished in sixteen out of nineteen rationed towns. Price controls on a number of consumer goods were also lifted over this period.

Against these favourable trends, certain disquieting features were discerned. Money supply increased substantially leading to a significant rise in prices and cost of living. The rise in money supply occurred notwithstanding the fact that for the first time in several years the Government sector did not add to it. This was a development which we consider of much significance. It was the outcome of the natural policy of a Government to live within its means and to avoid borrowing from our State Bank. Despite such contractionary influences of the Government sector, money supply rose by Rs. 29.60 crores compared to the rise of Rs. 19.79 crores in the preceding year. The increase was occasioned largely by the monetization of the balance of payments surplus. The rise in bank credit to the private sector was also an important causative factor. The increase in bank credit was mainly a consequence of a higher level of imports and a larger demand for funds following the transfer of trade in foodgrains to private hands. The rise in prices and cost of living reflected the inadequacy of supplies in relation to monetary demand. The increase in industrial production added only partly to domestic availabilities as substantial exports of manufactured goods took place under the Export Bonus Scheme. Some relief was provided by the rise in private account imports and a larger inflow of goods under commodity aid.

Even in sectors showing improvement, there were certain underlying trends which do not permit us scope for complacency. For instance, the increase in food production was the result mainly of favourable weather conditions and crop substitution, not especially to any concentrated effort on the part of the grower. As a result of sustained Government measures to expand agriculture the acreage under rice increased by 1.6 million to 24.1 million during 1959-60 but the yield per acre allowing for weather variations remained disappointingly low. As for wheat, production in 1959-60 at 3.9 million tons was actually less than in 1948-49 though the acreage under wheat during this period increased by about 2 million. There can be no hope of lasting improvement in food production unless basic agricultural problems are tackled in earnest and yields per acre show significant increase.

So far as the external financial position is concerned, the improvement over the whole year conceals a significant reversal of trends which set in during the second quarter of 1960. It is also to be remarked that by far the largest contribution to the rise in foreign exchange receipts has taken place by the export of manufactured goods under the Export Bonus Scheme. That earnings from conventional exports, namely jute and cotton, actually declined by Rs. 8 crores during 1959-60 underlines this point. Nevertheless, whatever the overall improvement the situation is that this Scheme can at best be considered as a temporary expedient. A real and lasting improvement, in our view, can take place only by raising the exportable surplus of our agricultural products and by increasing the competitive efficiency of our industries. Our exports of manufactured goods have shown a substantial rise in recent months, but in so far as the increase has been due to the incentive provided by the Export Bonus Scheme it is only a rather short-term gain. Larger exports of manufactured goods under artificial stimuli have not led my Government to believe that our domestic industry has secured a firm basis in the international market.

Also, improvement in the productive efficiency of our industries depends on the extent to which they can stand world competition without the support of such devices as the Expert Bonus Scheme. A careful study of cost structure is, therefore, of paramount importance. It would be quite suicidal on the part of manufacturers to remain complacent about the urgent need for improving their productive efficiency. The growth of industries in a highly sheltered market is certainly not a sure sign of economic strength. Sooner or later these industries will have to face world competition and that will be the time when they will have to meet the moment of truth. They can hold on to their gains only if they give sufficient attention to the rationalization of the cost of structure and to improvement in the quality of their products.

It is, in our thinking, of vital importance to concentrate on objectives which will bring about lasting improvements in the economy and to work for their attainment through consistent and integrated economic policies. The real solution to our problems lies in increasing production, both in agriculture and in industry. By releasing foreign exchange for the full utilization of capacity in a large number of industries and for the balancing and modernization of existing units, the Government of Pakistan have taken a large step towards expanding industrial output. The formulation of a "crash" programme for agriculture which focusses administrative energies on selected areas in the country represents a further advance and promises more expeditious results than what a thin spreading of effort over the whole country would have ensured. The success of the programme will depend upon how well the improvement can be sustained, especially when the focus of energy shifts, as it eventually must, to other areas.

It should be clearly understood that the problem of higher production is closely related to human incentive, and unless we at home are willing to provide the proper stimuli to the producer, the outcome might not reach expectations. Obviously we cannot expect proper response if policies in related fields are not conducive to such incentives.

Recently Government have moved in the right direction in raising the ceiling price of wheat by rupees three per maund (one maund is equivalent to 82 2/7 lbs.) and by removing the restriction on its movement in the country. Assuming that the marketing system will permit the farmer to obtain a fair proportion of this increase in price, it could be expected that he will raise the output, but whether he will actually react favourably does not depend entirely on the relaxation or removal of State controls. The danger is that unless the grower finds in the market commodities which he would like to exchange for his produce he may still remain indifferent to the need for producing more or for increasing the marketable surplus in proportion to increased production. In other words, it would be necessary to bring within his reach a sufficient supply of what he called "inducement goods" before he can be called upon to reinforce his efforts to produce more and to sell more.

The viability of the balance of payments is another important objective of our national effort. This objective can be attained only by increasing production and thereby enlarging the exportable surplus, although it depends in

no small measure on policies which influence the division of output between the home and the export market. Here, however, a conflict of policy objectives commences to operate. Under conditions of excess demand any increase in production tends to be absorbed by the home market unless action is taken to curb domestic consumption, which in turn leads to supply shortages and higher prices. This type of conflict continues until a sufficiently high level of production is achieved to feed both the internal as well as the external market. In the meantime the situation is met by resorting to temporary expedients. A typical example of this is the treatment of cotton yarn which is required internally and is also saleable abroad. To push our exports, cotton yarn was put under the Bonus Scheme about a year ago, but when exports started to move, the home market began to feel the pinch, and action was necessary to reduce severely the bonus entitlement to fifty per cent of the original and at the same time to control and reduce the prices of both yarn and finished products. The latter measure made the internal market less lucrative and strengthened the incentive for these items to move out. Ultimately the solution was found in asking each textile mill to supply a prescribed quantity of yarn to the domestic consumer, and as a result of this some equilibrium was restored. A similar case, though differing in some details, is that of tea exports.

My intention in citing these instances is two-fold. In the first place I should like to assure the Committee that there is no lack of effort on the part of my Government to make adjustments according to the changing conditions so characteristic of a developing economy. In the second place to consider the necessity to emphasize the desirability of striking balance between competing objectives and as far as possible of resolving the conflict among them through consistent policies within a well-articulated system of national priorities.

Pakistan's resources being limited, it is necessary that in addition to sector-wise priorities expressed in general terms to work out priorities on a project-by-project basis. This is most essential at the present juncture when the development programme embodied in the Second Five Year Plan is under way. The determination of correct priorities becomes all the more necessary when it is realized that the resources, our own as well as those likely to be made available to the country, are susceptible to change. This means that an adequate measure of flexibility and manoeuvrability in the Plan is essential. The alternative of proceeding indiscriminately on the entire front and making commitments in advance of foreign assistance is a method which Pakistan has scrupulously avoided in the past and would not like to follow in the future.

I have spoken for sufficient length of time already, I will try to summarize.

The economic situation in the country was generally favourable during 1959-60 except for the rise in prices and cost of living. Prices of major export commodities, cotton and jute, rose during the year owing to the supply position at home and improved foreign demand. Food production recorded a marked increase during the year due mainly to favourable weather conditions. Industrial production increased at a rate faster than last year. During the year under

report, Government's financial transactions, taking into account the effect of the counterpart funds, exercised a net contractionary influence of Rs. 3.39 crores on money supply as compared with the expansionary influence of Rs. 19.05 crores in 1958-59. However, owing to the sizeable surplus in the country's international accounts and rise in bank credit to the private sector, money supply rose sharply by Rs. 29.60 crores during 1959-60 compared to Rs. 19.79 crores in the preceding year. As a result of the increase in money supply and other factors such as larger exports of manufactured goods and progressive lifting of price controls, there was some rise in the general level of prices. In the external sector, the current account surplus in the balance of payments rose sharply from Rs. 1.36 crores in 1958-59 to Rs. 12.72 in 1959-60 owing to reduction in Government expenditure abroad and higher receipts from exports. The gold, dollar and sterling reserves rose by Rs. 12.65 crores to Rs. 116.96 crores during the course of the year.

ANNEX II

IMF Executive Board Decision of 4 November 1959
relating to Pakistan

1. The Government of Pakistan has consulted the Fund under Article XIV, Section 4, of the Fund Agreement concerning the further retention of its transitional arrangements.
2. Since late 1958 there has been a considerable improvement in Pakistan's economic situation. The Government has taken action on the budget problem with a view to eliminating inflationary financing. The level of taxation has been increased and it appears that any monetary impact of the 1959/60 budget will be small. Other measures that have been taken include an export Bonus Scheme to encourage minor exports, the granting of an amnesty to permit repatriation of foreign assets held illegally, an increase in the discount rate of the State Bank, and recently, a reduction in the scope of price controls. Exchange reserves, which had fallen to a low level, have risen at the same time that foreign liabilities were being reduced. There has been an increase in foreign assistance in dealing with the balance of payments and budgetary problems.
3. The Export Bonus Scheme as introduced in January 1959 gives rise to multiple currency practices. This Scheme recognizes the need for additional incentive for some exports, but it has certain undesirable effects. It, however, applies only to a small segment of the exchange market, and Pakistan has assured the Fund that the Scheme will be reviewed in the near future and that exchange policy continues to be based on the objective of having a unitary rate structure. The Fund does not object to these practices on a temporary basis.
4. The Fund welcomes the progress that has been made in reducing inflationary pressures, but notes that reliance on restrictions continues to be great. While the scope of bilateral arrangements does not appear to have been increased, Pakistan continues to practice some discrimination as a result of these arrangements. Otherwise import licensing is on a non-discriminatory basis. The Fund urges the consideration of policies which will reduce reliance on restrictions and discrimination and make possible the eventual unification of the rate structure.
5. In concluding the 1959 consultations, the Fund has no other comments to make on the transitional arrangements maintained by Pakistan.